

Red Owl Stores, Inc. Annual Report for period ended Feb. 27<sup>th</sup>, 1965

**ABOUT THE COVER:** *This was an exciting year for Red Owl . . . a year that saw record sales, record earnings, the opening of 14 new stores, the unique "red carpet" treatment, televised Bingo games and general growth and expansion in a variety of areas. To capture this excitement and variety, Roger Lundquist, a leading Upper Midwest artist, created this striking collage for our cover . . . a potpourri of some of the ideas and incidents that contributed to our past year.*





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*The annual stockholders' meeting will be held on June 1, 1965 at the office of the Corporation. A proxy statement and form of proxy will be mailed about May 1, 1965.*



THE RED OWL RED CARPET was rolled out last January in this luxurious new Red Owl Store in Denver. This "red carpet treatment" is the first of its kind anywhere. The entire sales area of this 17,000 square foot store is carpeted to make shopping more pleasurable.

## Highlights

### FISCAL YEAR ENDED

	Feb. 27, 1965	Feb. 29, 1964	Percentage Increase (Decrease)
Retail Sales . . . . .	\$242,544,633	\$236,994,194	2.3%
Agency and other wholesale sales . . . . .	61,951,579	59,075,999	4.9%
Total. . . . .	\$304,496,212	\$296,070,193	2.8%
Earnings			
Net earnings for the year . . . . .	\$ 3,042,239	\$ 2,768,398	9.9%
Reinvested in business . . . . .	\$ 1,622,739	\$ 1,418,257	14.4%
Earned per share common . . . . .	\$ 2.04	\$ 1.87	9.1%
Number of shares outstanding. . . . .	1,491,681	1,480,221	.8%
Dividends per share . . . . .	\$ .95	\$ .90	5.6%
Net working capital* . . . . .	\$ 16,550,648	\$ 16,867,889	(1.9)%
Ratio of current assets to current liabilities*. . . . .	1.97 to 1	2.02 to 1	
Book value per share common. . . . .	\$ 19.27	\$ 18.29	

\*Excluding wholly-owned realty subsidiaries





*To our  
shareholders  
and  
employees*



For the first time in your Company's history, consolidated sales exceeded \$300,000,000; earnings after taxes were more than \$3,000,000; and earnings per share surpassed the \$2 level.

Total sales for the year ended February 27, 1965, were up 2.8%, amounting to \$304,496,212 compared with \$296,070,193 in the prior fiscal year. New store expansion, continued growth of the franchised Agency Division, and an aggressive sales promotion program in our Snyder drug stores—all contributed to the growth in volume. These favorable factors more than offset a sales decline in some existing units particularly affected by local competitive and economic conditions.

Consolidated net earnings amounted to \$3,042,239 as compared to \$2,768,398 in the prior year. On a per share basis, earnings were \$2.04 versus \$1.87, an increase of 9.1%. There were 1,491,681 shares outstanding at the year end, or 11,460 more than a year earlier. Shares issued in connection with the conversion of debentures and the exercise of stock options somewhat exceeded the 17,000 additional shares purchased for the treasury during the year.

As a result of a higher quarterly payment beginning November 15, 1964, dividends for the fiscal year aggregated 95 cents against 90 cents per share the previous year. Currently, the Company's dividend is at the rate of \$1.00 annually. This action reflects the Board of Directors' general policy of increasing dividends as the level of earnings rises.

Fourteen new stores, counting replacements, were opened during the year including a 44,000 square foot Family Center and a Snyder drug store. Four of the new supermarkets were additions to Red Owl's Denver operations and another was opened in that metropolitan area shortly after the close of the fiscal year.

Objectives for the year ahead include the development of fifteen new or replacement stores, of which two are tentatively planned to be combination Red Owl supermarket-Snyder drug store units. Also, plans are under way for another large Family Center in the Twin City suburban area.

We are actively seeking other radio stations as a means of expansion by diversification. Our experience in this type operation has developed further interest in acquiring more broadcasting facilities. An application has been filed with the Federal Communications Commission for a license to operate a station in the Duluth-Superior area. If this and other current plans materialize, the Company could be operating several radio stations in the near future.

Although the expansion and acquisition programs for the year ahead will be financed principally by retained earnings, some additional funded debt is also contemplated.



Severe weather conditions adversely affected your Company's retail sales during the early weeks of the new fiscal year. Nevertheless, the over-all outlook for the year, at this time, appears encouraging and favorable both from the standpoint of sales and earnings results.

CHAIRMAN OF THE BOARD

PRESIDENT





*AGENCY OPERATORS met at The Food Show sponsored by Red Owl in April, 1965. To assist these men in improving their store operations, discussions were held concerning new products, new equipment, and new merchandising techniques and plans for the future.*

## *Review of the year's operation*

### **SALES EXCEEDED 300 MILLION FOR THE FIRST TIME.**

Consolidated sales for the fiscal year ended February 27, 1965, were \$304,496,212, as compared to \$296,070,193 in the previous year, an increase of 2.8%. Retail sales showed an increase of 2.3% while sales to Agency and other wholesale accounts were up 4.9% over the prior year.

### **EARNINGS AT NEW RECORD IN EXCESS OF 3 MILLION.**

Benefiting from the reduction in income tax rates and the adoption of the flow through method of handling the investment credit, consolidated net earnings after taxes reached a new high of \$3,042,239, or \$2.04 per share of common stock outstanding at the year-end, compared with the previous peak of \$2,768,398, equal to \$1.87 per share a year earlier.

The flow through method of handling the investment credit was adopted for the reason that expenditures for new equipment do not fluctuate sharply from year to year, and therefore permit the use of this more simplified accounting treatment. The flow through method appears to have become the generally accepted procedure for handling this tax adjustment within the industry.

A total of 28,460 shares of common stock were issued in connection with the conversion of debentures and the exercise of stock options. These additional shares were offset in part by the Company's purchase in the open market of 17,000 shares held in the treasury. At

the year end, total treasury shares amounted to 47,000 which are available for corporate purposes including possible future acquisitions.

**DIVIDENDS CURRENTLY AT \$1 ANNUAL RATE.** Effective with the November 15, 1964, payment, the Board of Directors increased the quarterly dividend from 22½ to 25 cents per share. Total payments for the fiscal year were 95 cents per share compared to 90 cents in the previous year. As shown on the ten year summary, Red Owl dividends have advanced from 60 cents per share to the new \$1.00 annual rate as earnings have grown during the period.

**SUPERMARKET EXPANSION CONTINUES.** Although Red Owl's future growth will be influenced by diversification, supermarket operation remains the Company's principal business. The largest portion of expansion effort is concentrated on this segment of the operation. During the year, twelve new supermarkets, including relocations, were opened. Of the new locations, four are in the Denver metropolitan area, thus marking the most rapid new store development in that market since acquiring that division five years ago.

During the year under review, twenty-eight existing stores received major or extensive remodelings and renovations. This program is in accordance with the Company's policy of keeping its store operations modern in appearance.

**AGGRESSIVE MERCHANDISING PROGRAM FOR SNYDER DRUG STORES.** At this time there are 26 Snyder drug stores in operation, plus three prescription departments in Family Centers. During the latter half of the fiscal year, an intensified program stressing low mark-up on certain items was initiated to increase traffic and store-wide volume. Results to date have been encouraging and further refinements and extension of this program will be made in the year ahead. Plans are also under way to open a prescription department in an existing Red Owl supermarket in Denver.

Red Owl's data processing facilities will be used to maintain Snyder's inventory records, and the program is now in the process of installation. It is expected this procedure will reduce costs, lower investment in inventory, and improve service to stores.

**FAMILY CENTER OPERATIONS.** In April 1964, the first large Family Center was opened in Coon Rapids, near the Twin Cities. This experiment, coupled with two outlying smaller units, has provided an opportunity to evaluate the merchandising potential for many lines not generally handled in a typical Red Owl supermarket. The Family Center concept has utilized the supermarket capabilities of Red Owl's personnel combined with the extensive non-food knowledge and experience of Snyder's organization. Progress thus far has been very encouraging.

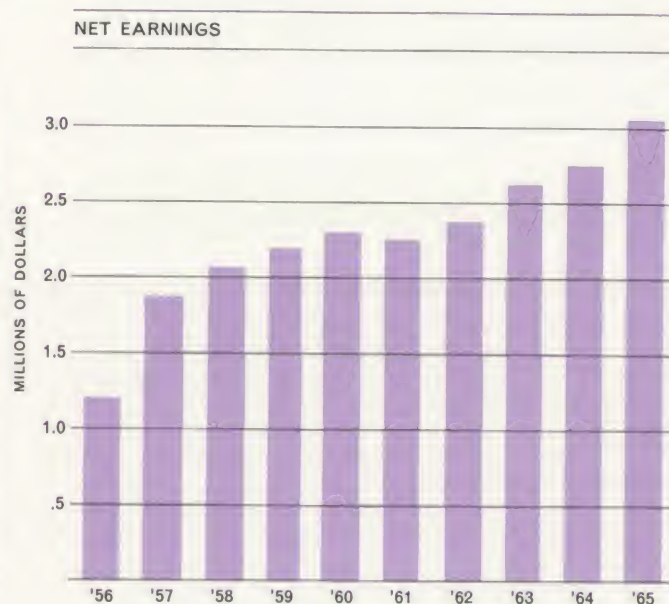
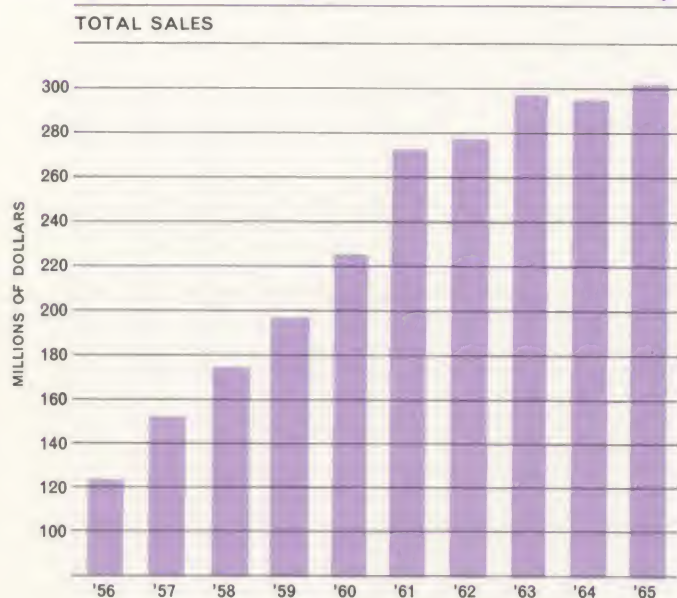
The land for another major Family Center has been purchased by a Red Owl subsidiary which will develop this project and secure tenants for other shops. Its final completion may extend into the following year.

*(Continued on next page)*

<i>Facilities</i>	IOWA	MICH.	MINN	MONT.	NO. DAK.	SO. DAK.	WISC.	WYO.	COLO.	TOTAL
Corporate Stores	3	9	72	2	19	18	35	2	18	178
Agency and Wholesale Accounts	8	19	122		49	25	70		181	474
Drug Stores			25				1			26
Principal Warehouses			2		1		1		1	5



# Comparison of sales, earnings, dividends and book values



**OUTLOOK ATTRACTIVE FOR FRANCHISED AGENCY OPERATIONS.** The franchise division which services Agency stores commenced operations in 1937. This phase of the business has shown consistent growth, produced a good return on investment, and offers a good opportunity for profitable expansion. At the fiscal year-end, Red Owl serviced 293 Agency franchised accounts in communities in which company-owned supermarkets are not located. Future plans call for extending this operation through growth in the areas now served, and the possibility of acquiring other companies in contiguous territory.

In addition to the Agency Division, Red Owl operates a Wholesale and a Cash and Carry business in the Denver area, which was acquired in 1960 in connection with the purchase of the assets of H. A. Marr Company. This segment showed a considerable gain in volume the past year and continues to be a profitable adjunct to operations in the Colorado division.

**PROCESSING OPERATIONS IMPORTANT.** For years Red Owl has supplied a large portion of its own bakery goods requirements. Currently, it operates eight bakeries of which four are located in the principal warehouses and serve numerous stores. The others are in-the-store type and each services from two to four units. A large coffee roasting and tea packing department in Hopkins supplies private label merchandise throughout the entire chain. The Company does considerable candy and nut packaging, operates a central packaging facility for meat and cheese, and a delicatessen manufacturing unit. The new, modern egg production plant was extended to full capacity during the year, and is now supplying uniform eggs of the highest quality to all Twin City stores.

**OTHER SERVICE ACTIVITIES.** The Hopkins warehouse

was completely re-aligned and re-equipped during the past year to improve its efficiency and to permit the handling of the added tonnage which flows through this building each year. It is anticipated that a similar modification will take place in at least one more warehouse in the year ahead.

A new concept for stocking stores, which has as its objective the reduction of inventories and the lowering of handling costs, was extended during the year and will be installed in a large number of other stores in the coming year.

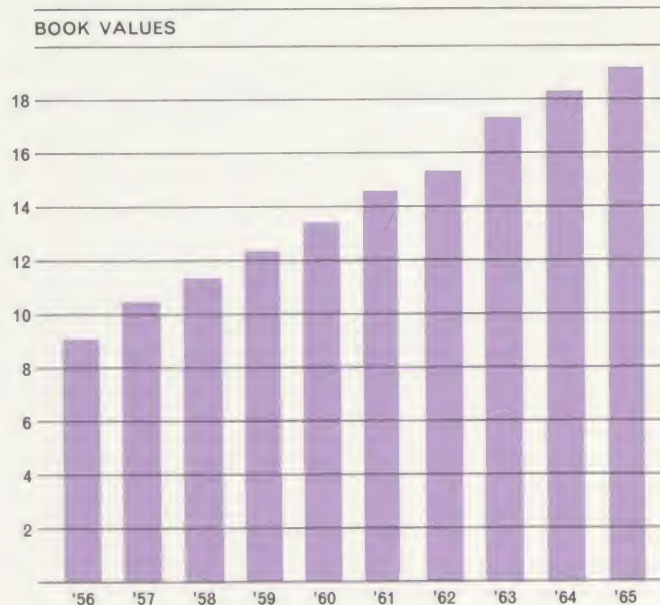
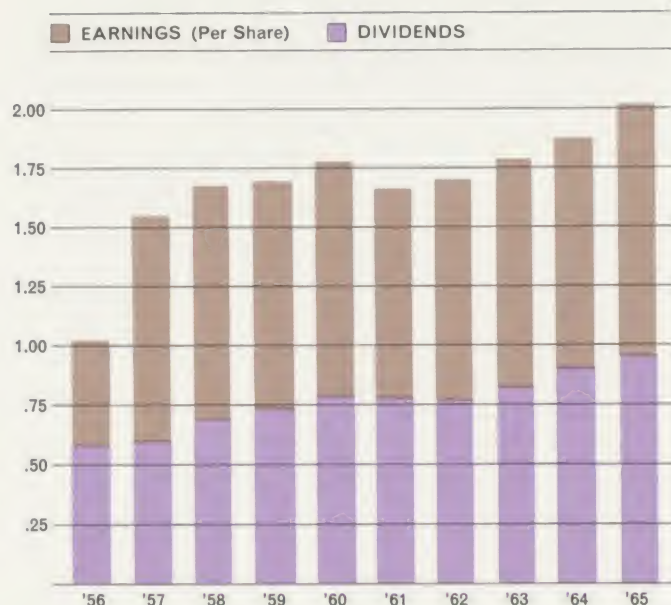
The key people in each of the Company's major departments work hand-in-hand with the Industrial Engineering staff to improve various phases of material handling and production.

Increasing use is being made of the electronic data processing equipment. High-speed transmission facilities link the Fargo and Green Bay warehouses with the central computer in Hopkins for order filling and billing. Further steps are being taken to implement the IMPACT program for scientific control of warehouse inventories. Objectives of this program are to lower warehouse inventory investments, improve service by less out-of-stock items, and reduce clerical costs associated with procurement.

**SUCCESSFUL RADIO STATION VENTURE TO BE EXPANDED.** Early in 1961, Red Owl acquired and has operated radio station KRSI located in suburban Minneapolis and serving the Twin City area. Since this purchase, the station has been authorized to broadcast full time, has secured a major network affiliation, and added FM facilities. Revenues of this station have been substantially expanded and it has made a significant contribution to earnings in each of the past two years.

Recently Red Owl submitted an application to the





Federal Communications Commission to operate a radio station in the Duluth-Superior area. This appears to be a logical location to extend the broadcasting activities and does not involve a substantial commitment of funds.

As a result of the favorable experience with KRSI, Management is also seeking other desirable broadcasting stations and is of the opinion that such additional facilities could be very significant in the Company's diversification plans.

**FINANCIAL POSITION.** Aside from acquisitions made through issuance of common stock, Red Owl has utilized internally generated sources of funds for all of its expansion since 1961, when it last received the proceeds from long-term debt financing. The Company's financial position remains strong. It may be necessary to secure some additional capital through debt financing to carry out the coming year's expansion and acquisition plans. During the past three years, the long-term debt has been reduced from over \$8,900,000 to its current level under \$6,000,000. This provides considerable flexibility in meeting the financial needs for continued growth of the Company.

Net working capital at year-end was \$16,550,648, compared with \$16,867,889 a year earlier. Expenditures for fixtures, equipment and leaseholds were \$4,116,619 while depreciation and amortization amounted to \$2,568,215.

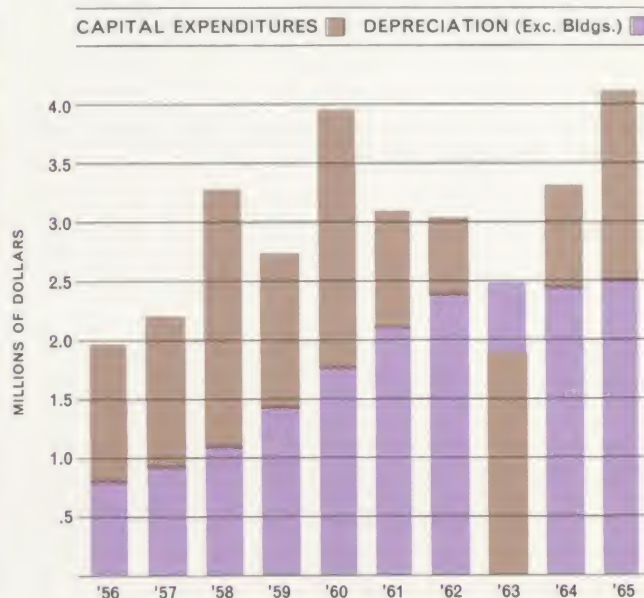
**ORGANIZATION MATTERS.** During the year Mr. Neil Elkey was elected Vice President and given responsibility for all wholesale activities. Mr. Elkey, an employee of sixteen years' service, previously headed the retail division in Wisconsin. Mr. Richard C. Johnson was elected Assistant Secretary and continues as Associate Counsel. He has been with Red Owl since 1957.

Mr. T. R. Anderson was added to the Board of

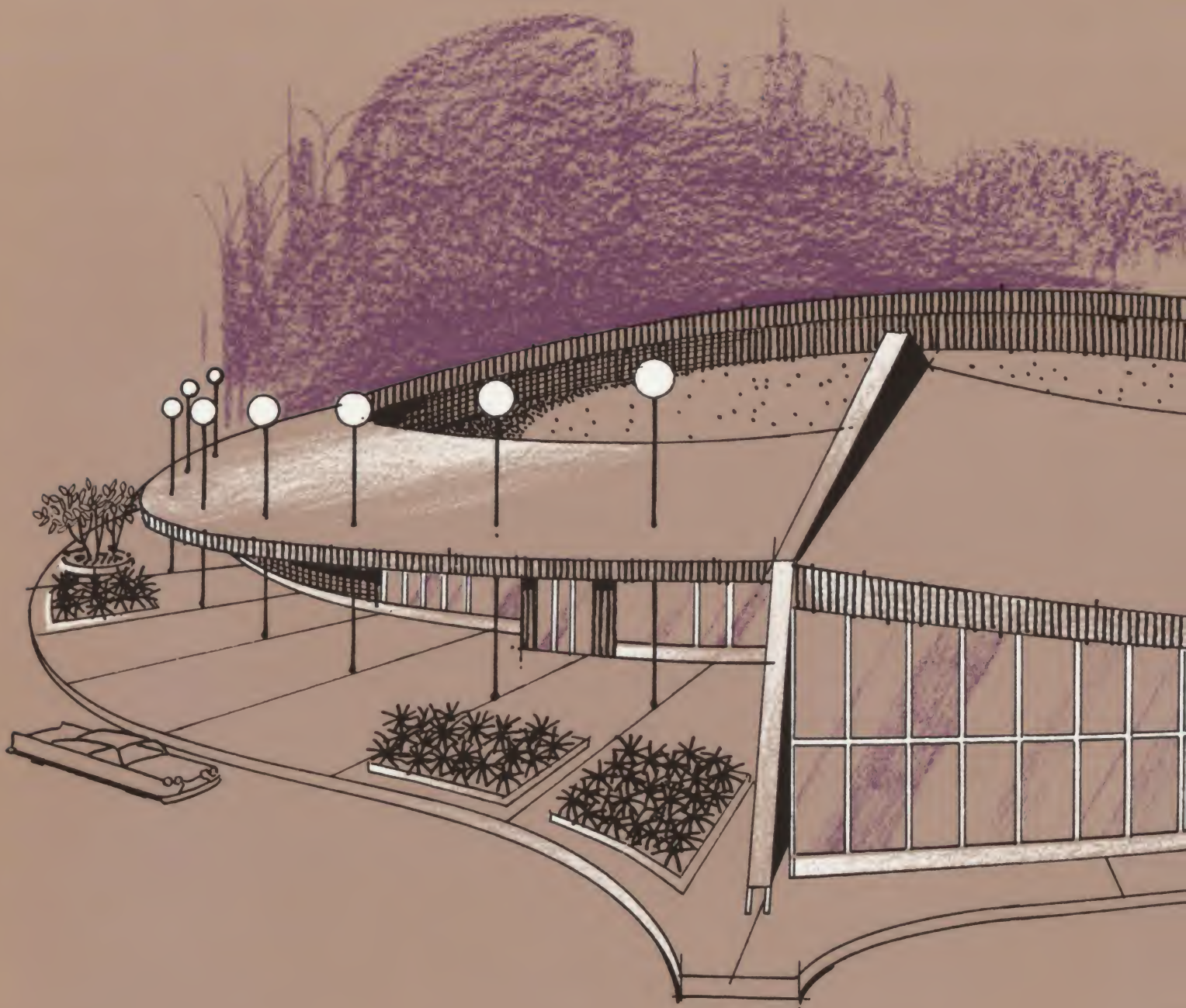
Directors at the last annual meeting. He is a Minneapolis resident with numerous business interests. Mr. William J. Quinn, Vice President of Red Owl since 1955 was elected to the Board of Directors on July 1, to fill a vacancy which occurred at that time.

Considerable attention is given to training personnel to prepare them for positions of greater responsibility as the Company grows, as well as to improve their skills and abilities.

The group insurance program was amended recently at Company cost to provide major medical coverage for eligible employees. All benefits are reviewed regularly in an attempt to keep plans up to date and maintain good employee relations.







## *Looking ahead*

Pictured above is an architectural rendering of another major Family Center planned for the coming year in the suburban Twin City area.

Supermarket and drug store expansion in the coming

year is anticipated to be at a somewhat greater pace than in the past year. Agency and wholesale volume will be sought after more aggressively than heretofore.

The search for better and more effective ways of





operating the various segments of the Company will continue. In recent years, Red Owl's growth has included a certain degree of diversification, although the retail and wholesale food business remains its princi-

pal endeavor. Management will, as before, devote considerable time to evaluating acquisitions not only in its present field but in related areas which may have beneficial implications.

## *Red Owl Stores, Inc. and Consolidated Subsidiaries*

### Consolidated Statement of Operations and Retained Earnings Year ended February 27, 1965 (with comparative figures for the previous year)

	YEAR ENDED	
	Feb. 27, 1965	Feb. 29, 1964
Net sales:		
Retail . . . . .	\$242,544,633	236,994,194
Wholesale . . . . .	61,951,579	59,075,999
Total net sales . . . . .	304,496,212	296,070,193
Costs and operating expenses:		
Cost of goods sold, including warehousing and transportation expenses . . . . .	249,497,468	242,982,670
Selling, general and administrative and other operating expenses . .	49,260,744	47,180,823
Total costs and operating expenses . . . . .	298,758,212	290,163,493
Operating earnings . . . . .	5,738,000	5,906,700
Other deductions (income)—net:		
Interest (on long-term debt . . . . .	389,596	443,462
(other . . . . .	3,259	3,729
Miscellaneous deductions . . . . .	219,862	160,554
Loss (gain) on disposal of property and equipment—net . . . . .	22,867	(42,804)
Miscellaneous income . . . . .	(154,170)	(250,515)
Total other deductions (income)—net . . . . .	481,414	314,426
Earnings before taxes on income . . . . .	5,256,586	5,592,274
Federal and State taxes on income, estimated (note 3) . . . . .	2,411,000	2,980,000
Net earnings before undistributed earnings of wholly-owned realty subsidiaries . . . . .	2,845,586	2,612,274
Net earnings of wholly-owned realty subsidiaries . . . . .	196,653	156,124
Net earnings . . . . .	3,042,239	2,768,398
Deduct dividends on Red Owl Stores, Inc. common stock— \$.95 and \$.90 per share in respective years . . . . .	1,419,500	1,350,141
Retained earnings at beginning of year—unappropriated . . . . .	1,622,739	1,418,257
Retained earnings at end of year:	16,396,876	14,978,619
Unappropriated (notes 1 and 4) . . . . .	18,019,615	16,396,876
Appropriated for possible future inventory losses . . . . .	285,000	285,000
Total at end of year . . . . .	\$ 18,304,615	16,681,876

See accompanying notes to financial statements.



# Red Owl Stores, Inc. and Consolidated Subsidiaries

## Consolidated Balance Sheet

February 27, 1965 (with comparative figures for the previous year)

<b>Assets</b>	<u>Feb. 27, 1965</u>	<u>Feb. 29, 1964</u>
Current assets:		
Cash and certificates of deposit . . . . .	\$ 3,388,793	5,081,679
Marketable securities, at cost plus accrued interest (approximate market) . . . . .	99,828	995,710
Accounts and notes receivable, less allowance for doubtful receivables \$86,006 . . . . .	2,886,110	2,552,374
Merchandise inventories (note 2) . . . . .	26,147,762	23,684,185
Prepaid expenses . . . . .	<u>1,131,137</u>	<u>1,148,637</u>
Total current assets . . . . .	33,653,630	33,462,585
Investments and other assets:		
Investments in and advances to wholly-owned realty subsidiaries not consolidated, at net equity value (note 1) . . . . .	2,417,535	2,639,685
Miscellaneous . . . . .	<u>982,817</u>	<u>1,009,172</u>
Total investments and other assets . . . . .	3,400,352	3,648,857
Property, plant and equipment, at cost less depreciation and amortization (note 3) . . . . .	14,997,288	13,741,193
Deferred charges . . . . .	1,074,508	1,024,547
Radio station license and goodwill, at cost . . . . .	<u>243,383</u>	<u>243,383</u>
	<u>\$53,369,161</u>	<u>52,120,565</u>
<b>Liabilities</b>		
Current liabilities:		
Current instalments of long-term debt . . . . .	\$ 715,000	715,000
Accounts payable . . . . .	10,209,113	9,330,598
Accrued expenses . . . . .	4,952,050	4,627,269
Federal and State taxes on income, estimated . . . . .	<u>1,226,819</u>	<u>1,921,829</u>
Total current liabilities . . . . .	17,102,982	16,594,696
Deferred Federal taxes on income and investment credit (note 3) . . . . .	1,544,040	1,453,556
Long-term debt, less current instalments included above (note 4) . . . . .	5,977,000	6,999,000
Stockholders' equity:		
Preferred stock—par value \$100 per share. Authorized 50,000 shares; none outstanding . . . . .	—	—
Common stock—no par value, stated value \$1.50 per share. Authorized 3,000,000 shares; issued 1,538,681 shares (1,510,221 in 1964) (note 5) . . . . .	2,308,022	2,265,332
Additional amounts paid in by stockholders (note 6) . . . . .	9,315,528	8,838,605
Retained earnings (notes 1 and 4), per accompanying statement . . . . .	<u>18,304,615</u>	<u>16,681,876</u>
	29,928,165	27,785,813
Less common stock held in treasury, 47,000 shares (30,000 shares in 1964), at cost . . . . .	<u>1,183,026</u>	<u>712,500</u>
Total stockholders' equity . . . . .	28,745,139	27,073,313
Commitments (note 7) . . . . .	<u>\$53,369,161</u>	<u>52,120,565</u>

See accompanying notes to financial statements.

# Wholly-owned Realty Subsidiaries of Red Owl Stores, Inc.

## Combined Balance Sheet February 27, 1965 (with comparative figures for the previous year)

	Feb. 27, 1965	Feb. 29, 1964
<b>Assets</b>		
Cash . . . . .	\$ 187,654	54,752
Accounts receivable . . . . .	767	18,342
Prepaid expenses . . . . .	297	2,626
Property and plant, at cost less depreciation (note 3) . . . . .	7,684,871	8,977,523
Deferred charges . . . . .	41,305	60,274
	<u>\$7,914,894</u>	<u>9,113,517</u>
<b>Liabilities</b>		
Current instalments of long-term debt . . . . .	\$ 384,860	403,765
Accounts payable and accrued expenses . . . . .	12,707	127,109
Federal and State taxes on income, estimated . . . . .	116,015	91,064
Due to Red Owl Stores, Inc. . . . .	1,322,716	1,741,519
Deferred Federal taxes on income and investment credit (note 3) . . . . .	273,715	231,654
Long-term debt, less current instalments above (note 4) . . . . .	4,710,062	5,620,240
Investment of Red Owl Stores, Inc.:		
Capital stock . . . . .	130,000	130,000
Additional paid-in capital . . . . .	54,000	54,000
Retained earnings, per statement below . . . . .	910,819	714,166
	<u>1,094,819</u>	<u>898,166</u>
	<u>\$7,914,894</u>	<u>9,113,517</u>

## Combined Statement of Earnings and Retained Earnings Year ended February 27, 1965 (with comparative figures for the previous year)

	YEAR ENDED	
	Feb. 27, 1965	Feb. 29, 1964
Revenue and other income:		
Rents from Red Owl Stores, Inc. . . . .	\$ 857,428	822,222
Rents from others and miscellaneous . . . . .	162,505	147,154
	<u>1,019,933</u>	<u>969,376</u>
Expenses and other deductions:		
Depreciation and amortization . . . . .	299,238	287,451
Interest . . . . .	296,890	318,639
Amortization of debt expense . . . . .	6,913	8,366
Miscellaneous . . . . .	65,239	71,796
	<u>668,280</u>	<u>686,252</u>
Earnings before taxes on income . . . . .	351,653	283,124
Federal and State taxes on income, estimated (note 3) . . . . .	155,000	127,000
Net earnings . . . . .	196,653	156,124
Retained earnings at beginning of year . . . . .	714,166	558,042
Retained earnings at end of year . . . . .	<u>\$ 910,819</u>	<u>714,166</u>

See accompanying notes to financial statements.



*Source and use of funds* (with comparative figures for the previous year)

Year ended February 27, 1965

Red Owl Stores, Inc. and Consolidated Subsidiaries

	YEAR ENDED	
	Feb. 27, 1965	Feb. 29, 1964
Funds provided from:		
Net earnings before undistributed earnings of realty subsidiaries . . . . .	\$2,845,586	2,612,274
Depreciation and amortization of property . . . . .	2,568,215	2,496,606
Deferred income taxes and investment credit—net . . . . .	90,484	33,113
Decrease (increase) in investments in and advances to realty subsidiaries . . . . .	418,803	(533,856)
Sales and exchanges (repurchases) of common stock—net . . . . .	49,087	(492,950)
	<u>\$5,972,175</u>	<u>4,115,187</u>
Funds used for:		
Property and equipment additions—net:		
Buildings . . . . .	\$ 481	262,942
Fixtures, equipment and leasehold improvements . . . . .	4,116,619	3,317,096
Less net book value of dispositions . . . . .	(292,790)	(160,222)
	<u>3,824,310</u>	<u>3,419,816</u>
Cash dividends paid to stockholders . . . . .	1,419,500	1,350,141
Reduction in long-term debt, including debenture conversions . . . . .	1,022,000	1,004,100
Increase (decrease) in other assets—net . . . . .	23,606	(48,415)
Increase (decrease) in working capital . . . . .	(317,241)	(1,610,455)
	<u>\$5,972,175</u>	<u>4,115,187</u>

Wholly-owned Realty Subsidiaries of Red Owl Stores, Inc.

Funds provided from:		
Net earnings . . . . .	\$ 196,653	156,124
Depreciation and amortization of property . . . . .	299,238	287,451
Deferred income taxes and investment credit—net . . . . .	42,061	43,323
Net book value of land and buildings sold . . . . .	1,040,933	—
	<u>\$1,578,885</u>	<u>486,898</u>
Funds used for:		
Property and equipment additions:		
Land and buildings . . . . .	\$ 42,713	1,040,221
Equipment . . . . .	4,806	220
	<u>47,519</u>	<u>1,040,441</u>
Reduction in long-term debt . . . . .	910,178	403,765
Decrease (increase) in investment and advances by Red Owl Stores, Inc. . . . .	418,803	(533,856)
Increase (decrease) in other assets . . . . .	(18,969)	83
Decrease (increase) in working capital deficit . . . . .	221,354	(423,535)
	<u>\$1,578,885</u>	<u>486,898</u>

## Notes to Financial Statements Year ended February 27, 1965

**NOTE 1.** The accompanying consolidated financial statements include the accounts of Red Owl Stores, Inc. and all active subsidiaries except seven wholly-owned realty subsidiaries for which combined financial statements are included in this report. Consolidated financial statements proposed to be filed with the Securities Exchange Commission will fully consolidate all subsidiaries. In the accompanying consolidated financial statements, investments in and advances to unconsolidated wholly-owned realty subsidiaries are stated at the Company's equity in the net assets of such subsidiaries and their undistributed earnings are included in consolidated net earnings and retained earnings in the same net amounts as in fully consolidated statements. Differences in financial position as would be shown in a fully consolidated balance sheet, principally increases in property and long-term debt, may be obtained by combining the related captions in the accompanying consolidated and combined balance sheets and eliminating inter-company investments and advances.

**NOTE 2.** Merchandise inventories of dry groceries in retail stores are valued at the lower of cost or market determined by the retail inventory method; merchandise inventories in drug stores were valued at lower of cost or market at various dates during the last three months of the fiscal year and have been adjusted for transactions to February 27, 1965 on the basis of gross profit percentages; warehouse and other inventories are valued at the lower of cost (first-in, first-out) or replacement market. Details of merchandise inventories are as follows:

	1965	1964
Retail stores . . . . .	\$10,021,912	9,109,746
Warehouses . . . . .	14,878,125	13,336,799
Other and in transit . . . . .	1,247,725	1,237,640
	<u>\$26,147,762</u>	<u>23,684,185</u>

**NOTE 3.** Property, plant and equipment, at cost less depreciation and amortization, and related depreciation and investment credit policy are summarized as follows:

	RED OWL STORES, INC. AND CONSOLIDATED SUBSIDIARIES	WHOLLY-OWNED REALTY SUBSIDIARIES
Land . . . . .	\$ 386,178	1,404,652
Buildings . . . . .	717,122	7,020,464
Buildings on leased land . . . . .	—	505,534
Furniture, fixtures and equipment . . . . .	21,842,170	350,321
Automotive equipment . . . . .	4,004,747	—
	<u>26,950,217</u>	<u>9,280,971</u>
Less depreciation and amortization . . . . .	14,445,232	1,596,100
	<u>12,504,985</u>	<u>7,684,871</u>
Leasehold improvements, at cost less amortization . . . . .	2,140,321	—
Construction in progress and property held for sale . . . . .	351,982	—
	<u>\$14,997,288</u>	<u>7,684,871</u>

Depreciation charges against earnings have been computed by the straight-line method; for income tax purposes, however, depreciation on certain buildings and on fixtures and equipment acquired since 1954 has been computed by accelerated methods. Provision has been made for deferred income taxes applicable to the excess of depreciation claimed for tax purposes over amounts charged against earnings. Portions of deferred income taxes will be used to reduce provisions for Federal income taxes in future years when depreciation charges against earnings exceed amounts deductible for tax purposes.

The entire investment tax credit for the fiscal year 1965, \$185,690 for Red Owl Stores, Inc. and consolidated subsidiaries, has been included in earnings as a reduction in the provision for Federal taxes on income. Investment tax credits which were deferred in previous years are continuing to be amortized over the estimated lives of the related property. As a result of this change in method of accounting, net earnings of Red Owl Stores, Inc. and consolidated subsidiaries for 1965 were increased by approximately \$175,000.

**NOTE 4.** Long-term debt, less instalments due within one year and cash held by trustee for current redemptions, and related restrictions are summarized as follows:

	RED OWL STORES, INC. AND CONSOLIDATED SUBSIDIARIES	WHOLLY-OWNED REALTY SUBSIDIARIES
3½% notes due July 1, 1966 . . . . .	\$ 360,000	—
5½% notes due October 1, 1972 . . . . .	2,250,000	—
5¾% note due January 1, 1975 . . . . .	3,025,000	—
4¾% convertible subordinated debentures due February 1, 1978 . . . . .	342,000	—
6¼% mortgage note due October 15, 1975 . . . . .	—	242,140
5½% mortgage note due December 1, 1978 . . . . .	—	301,702



## Notes to Financial Statements (Continued)

	RED OWL STORES, INC. AND CONSOLIDATED SUBSIDIARIES	WHOLLY-OWNED REALTY SUBSIDIARIES
5¾% mortgage notes, \$785,661 due September 1, 1980, \$166,488 due August 1, 1981, \$355,460 due December 1, 1981, \$177,578 due June 1, 1982, and \$148,720 due March 1, 1983 . . . . .	—	1,633,907
Sinking fund mortgage bonds:		
4% due June 1, 1969, Series A . . . . .	—	213,500
4¼% due March 1, 1970, Series B . . . . .	—	134,000
4½% due December 1, 1975, Series C . . . . .	—	1,067,500
4¾% due December 1, 1977, Series D . . . . .	—	446,225
4¾% due December 1, 1982, Series E . . . . .	—	602,000
Equipment purchase contract due March 23, 1967 . . . . .	—	69,088
	<u>\$ 5,977,000</u>	<u>4,710,062</u>

Aggregate annual maturities and sinking fund requirements in the five fiscal years subsequent to February 26, 1966 for Red Owl Stores, Inc. and consolidated subsidiaries and wholly-owned realty subsidiaries, respectively, are as follows: 1967, \$835,000 and \$392,546; 1968, \$675,000 and \$335,569; 1969, \$675,000 and \$332,244; 1970, \$675,000 and \$299,997; 1971, \$675,000 and \$288,167.

The mortgage notes and sinking fund mortgage bonds are variously secured by warehouse and store properties and the wholly-owned realty subsidiaries' interests in related long-term leases to the Company. The 4¾% subordinated debentures are convertible into shares of the Company's common stock at \$16-2/3 per share, subject to adjustment under certain conditions.

Restrictions on payment of dividends (except stock dividends) and purchase, redemption or retirement of capital stock are imposed by the terms of agreements relating to the Company's 3¾% notes, 5½% notes, 5¾% note and 4¾% debentures. Retained earnings at February 27, 1965 free from restrictions, based on working capital and retained earnings requirements under the most restrictive of the agreements amount to approximately \$3,800,000.

**NOTE 5.** Of the authorized common stock, 20,520 shares are reserved for issuance upon conversion of the 4¾% subordinated debentures, 32,945 shares are reserved for issuance upon exercise of options granted under the Employees' Restricted Stock Option Plan and the Employees' Qualified Stock Option Plan; 33,970 shares remain available for granting of future options under the Employees' Qualified Stock Option Plan adopted June 8, 1964.

Under the new qualified plan, options are granted at not less than 100% (95% under old restricted plan) of market value at dates granted and become exercisable over a period of four years (five years under old restricted plan) commencing one year after dates granted. All options expire, subject to earlier expiration in the event of termination of employment, if not exercised within five years (six years under old restricted plan) of dates granted. Outstanding options have been granted at prices ranging from \$20.25 to \$31.25 per share (\$27.25 for qualified plan in 1964); at dates of grant, shares under option had an aggregate market value of \$763,250, an average of \$23.17 per share. Changes during fiscal year 1965 in stock options held by key employees are summarized as follows:

	OPTIONS GRANTED		OPTIONS EXERCISABLE	
	Shares	Amount	Shares	Amount
Balance at beginning of year . . . . .	45,475	\$1,006,809	19,015	\$438,224
Granted or became exercisable . . . . .	2,500	68,125	6,782	147,066
Exercised . . . . .	(10,040)	(218,293)	(10,040)	(218,293)
Cancelled or expired . . . . .	(4,990)	(121,572)	(3,708)	(93,975)
Balance at end of year . . . . .	<u>32,945</u>	<u>\$ 735,069</u>	<u>12,049</u>	<u>\$273,022</u>

**NOTE 6.** Additional amounts paid in by stockholders during the year aggregate \$476,923 as follows: excess of amounts paid in over stated value of 10,040 shares of common stock issued upon exercise of employees' stock options, \$203,233; excess of conversion price over stated value of 18,420 shares of common stock issued on conversion of 4¾% subordinated debentures, \$279,370, less applicable portion of unamortized debenture issuance expenses, \$5,680.

**NOTE 7.** Long-term leases, excluding leases to the Company by its wholly-owned realty subsidiaries, expiring more than three years after February 27, 1965, establish minimum annual rentals on 213 locations. The approximate minimum annual rentals under such leases, excluding taxes, insurance and maintenance costs payable by the Company, amount to \$4,230,000 (including \$556,000 applicable to properties sub-let). Of this amount, leases with minimum annual rentals of \$1,257,000 expire in fiscal years 1969 through 1973 and leases with minimum annual rentals of \$2,973,000 have terms extending into fiscal years 1974 through 1985.

Approximate minimum annual rentals on properties leased from wholly-owned realty subsidiaries aggregate \$842,000 (including \$203,000 applicable to properties sub-let).

In addition, the Company has entered into agreements to lease store properties at new locations for initial periods of seven to fifteen years at minimum annual rentals which will aggregate approximately \$218,000.

### Other commitment:

The Company's unfunded liability for past service benefits under the terms of a non-contributory salaried employees' pension plan, adopted November 12, 1959, amounts to approximately \$1,661,000 at February 27, 1965.



# Accountants' report

PEAT, MARWICK, MITCHELL & CO.  
CERTIFIED PUBLIC ACCOUNTANTS  
NORTHWESTERN BANK BUILDING  
MINNEAPOLIS 2, MINN.

## THE BOARD OF DIRECTORS AND SHAREHOLDERS RED OWL STORES, INC.:

We have examined the consolidated balance sheet of Red Owl Stores, Inc. and consolidated subsidiaries and the combined balance sheet of wholly-owned realty subsidiaries of Red Owl Stores, Inc. as of February 27, 1965, and related statements of operations, earnings and retained earnings for the year then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying balance sheets and statements of operations, earnings and retained earnings present fairly

the consolidated financial position of Red Owl Stores, Inc. and consolidated subsidiaries and the combined financial position of wholly-owned realty subsidiaries of Red Owl Stores, Inc. at February 27, 1965, and the results of the related operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year, except for the change to an accepted alternative method of accounting for the investment credit, as described in note 3 to the financial statements. Also, in our opinion, the accompanying summaries of source and use of funds for the year ended February 27, 1965 present fairly the information shown therein.

Minneapolis, Minnesota  
April 16, 1965

*Peat, Marwick, Mitchell & Co.*

## How the sales dollar was divided

86.3¢

for merchandise, transportation,  
handling costs

11.1¢

for wages, salaries,  
employee benefits

.8¢

for income  
taxes

.8¢

for depreciation  
of buildings  
and equipment

.5¢

to  
stockholders

.5¢

reinvested in  
future growth  
of company





## Directors

T. R. ANDERSON, President, Perrybell Enterprises, Inc. (Investment Co.)  
 JAMES R. ARNEILL, M.D., Executive Director and Chief Surgeon of Arneill Medical and Dental Center, Denver, Colorado  
 FORD BELL, Chairman of the Board of Directors, and Chief Executive Officer, Red Owl Stores, Inc.  
 ALF L. BERGERUD, Legal Counsel and Consultant  
 JOHN C. CORNELIUS, Senior Consultant and Director, Batten, Barton, Durstine & Osborn, Inc.  
 GLENN R. GRIFE, Retired (formerly Red Owl Stores, Inc.)  
 GOODRICH LOWRY, President, Northwest Bancorporation of Minneapolis  
 PIERCE H. McDOWELL, President, Howatt-McDowell, Inc., Sioux Falls, South Dakota  
 DONALD G. McNEELY, Vice President, St. Paul Terminal Warehouse Company of St. Paul  
 WILLIAM J. QUINN, Vice President, Red Owl Stores, Inc.  
 LAWRENCE W. RIXE, Vice President, Red Owl Stores, Inc.  
 JAMES A. WATSON, President Red Owl Stores, Inc.

## Officers

FORD BELL, Chairman of the Board of Directors and Chief Executive Officer  
 JAMES A. WATSON, President  
 NEIL ELKEY, Vice President, Agency and Wholesale Operations  
 MERLE R. GETTEN, Vice President, Retail Operations  
 MICHAEL J. McMAHON, Vice President, Advertising  
 WILLIAM J. QUINN, Vice President, Merchandising and Procurement  
 LAWRENCE W. RIXE, Vice President, Finance  
 VERNON J. WINTER, Vice President, Warehousing, Transportation and Manufacturing  
 JOSEPH T. SYDNESS, Secretary  
 THOMAS R. PELLETT, Treasurer  
 F. D. SCOTT, Controller  
 CLAYTON C. RaDUE, Assistant Vice President, Retail Operations  
 FRANK L. WALKER, Assistant Vice President, Agency Division  
 RICHARD C. JOHNSON, Assistant Secretary Associate Counsel

## Ten year record of growth

FISCAL YEAR ENDED IN	1965	1964	1963	1962	1961	1960	1959	1958	1957	1956
<i>(000's omitted)</i>										
Sales Retail . . . . .	\$242,545	\$236,994	\$244,016	\$228,343	\$222,647	\$187,957	\$165,662	\$144,891	\$124,293	\$ 95,074
Wholesale . . . . .	61,951	59,076	55,927	50,712	51,945	38,632	33,882	31,539	30,249	28,679
Total Sales . . . . .	304,496	296,070	299,943	279,055	274,592	226,589	199,544	176,430	154,542	123,753
<i>(000's omitted)</i>										
Net earnings for year . . . . .	3,042	2,768	2,653	2,374	2,248*	2,350	2,195	2,064	1,852	1,235
Dividends paid on Preferred Stock . . . . .	—	—	—	—	—	—	—	—	83	112
Net earnings applicable to common equity . . . . .	3,042	2,768	2,653	2,374	2,248*	2,350	2,195	2,064	1,769	1,123
Dividends paid on common stock . . . . .	1,419	1,350	1,217	1,110	1,078	1,048	936	854	664	598
Net earnings for year retained in business . . . . .	1,623	1,418	1,436	1,263	1,170*	1,302	1,259	1,210	1,105	525
Net earnings per share common . . . . .	2.04	1.87	1.77	1.69	1.65*	1.77	1.70	1.69	1.57	1.09
Dividends per share common . . . . .	.95	.90	.82½	.80	.80	.80	.75	.70	.62½	.60
Net Working Capital** <i>(000's omitted)</i> . . . . .	16,551	16,867	18,478	15,272	13,468	12,720	12,921	12,866	8,424	8,369
Ratio of current assets to current liabilities** . . . . .	1.97 to 1	2.02 to 1	2.23 to 1	2.14 to 1	2.12 to 1	1.98 to 1	2.25 to 1	2.37 to 1	2.06 to 1	2.24 to 1
Stockholders' Equity <i>(000's omitted)</i> . . . . .	28,745	27,073	26,148	22,146	20,214	18,247	16,351	13,986	12,738	11,604
Shares outstanding—Preferred . . . . .	—	—	—	—	—	—	—	—	9,500	18,850
Common . . . . .	1,491,681	1,480,221	1,498,106	1,404,266	1,363,732	1,330,232	1,291,992	1,221,782	1,123,722	1,027,802
Book value per share common . . . . .	19.27	18.29	17.45	15.77	14.82	13.72	12.66	11.45	10.45	9.37
Number of common shareholders . . . . .	4,123	4,249	4,182	4,078	4,183	4,290	3,827	3,228	2,389	2,291
Number of food stores at close of year										
Retail . . . . .	178	170	173	172	166	163	148	152	146	143
Agency and wholesale . . . . .	474	454	450	426	423	439	354	376	419	504
Total sq. ft. retail stores . . . . .	2,271,365	2,093,308	2,143,331	2,076,306	1,931,107	1,815,422	1,512,035	1,386,442	1,143,665	964,303
Number of employees (including part time) . . . . .	7,850	7,600	7,700	7,400	7,000	6,100	5,600	5,300	4,600	3,900

\*Excluding a special credit of \$294,000 in 1961.

\*\*Red Owl Stores, Inc. and consolidated subsidiaries excluding wholly-owned realty subsidiaries.

NOTE: Comparative figures have been adjusted, where applicable, for the two-for-one stock distribution on March 22, 1963 to holders of record on March 15, 1963.

For more information about the activities and policies of Red Owl Stores, write to . . . RED OWL STORES, INC., HOPKINS, MINNESOTA  
 EXECUTIVE OFFICES: 215 E. Excelsior Avenue, Hopkins, Minnesota. MAILING ADDRESS: Post Office Box 329, Minneapolis, Minnesota 55440.  
 STOCK TRANSFER AGENTS: Northwestern National Bank of Minneapolis, Bankers Trust Company of New York. REGISTRARS: First National Bank of Minneapolis; Morgan Guaranty Trust Company of New York. AUDITORS: Peat, Marwick, Mitchell & Co.



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### Ground Broken For Red Owl Store

Red Owl Stores, Inc. joined their future neighbors in groundbreaking ceremonies Thursday and announced plans for a 14,000-square-foot supermarket at the new boulevard shopping center at E. Iowa ave. and S. Colorado blvd.

Also participating in the grounds-breaking with plans to locate in the shopping center, were the Villages Inn, Panchito House, Panchito's Beauty Salon and Lebar's Pharmacy.

The shopping center property is owned by Eugene Reed, Joe Lutz and shopping center architect, planning to bring handling by S. Co.

He said the new store is one of several Red Owl intends to bring into the Denver area. John Mack, who manages the East Colfax ave. Villages Inn Panchito House, said the new supermarket in the Boulevard Shopping Center will cover about 14,000 sq. ft. and will be open for new Oct. 1.

The Frontier Business

RED OWL JUICE, CONCENTRATED  
GRAPE JUICE 7 6-OZ. CANS \$1.00

CONDENSED TOMATOES \$0.50

Head Let

2 FOR 2

FIRM, MEATY, VINE-RIPENED

Tomatoes

CRISP GREEN TOP

Red Radishes

SNAPPY, PENCIL THIN

Green Onions

RED OWL COLBY

Longhorn Cheese

50 50 EXTRA FREE

with purchase of 50

Penn



You'll